

RECEIVED

MAY 23 1997

MTG/DG
SPEAR STREET TOWER
ONE MARKET
SAN FRANCISCO
CALIFORNIA 94105

BROBECK
PHLEGER &
HARRISON
LLP
ATTORNEYS AT LAW

TELEPHONE: (415) 442-0900
FACSIMILE: (415) 442-1010
WRITER'S DIRECT DIAL:

(415) 442-1155

May 20, 1997

Michael Mazerov
Multistate Tax Commission
Suite 425
444 North Capitol Street, N.W.
Washington, D.C. 20001

Re: Issue Lists:
-- Uniform Definition of Unitary Business
-- Uniform Definition of Business-Nonbusiness Income

Dear Mr. Mazerov:

Thank you for copies of the two "issue lists" prepared in connection with the Business/Government Dialogue on State Tax Uniformity last November.

The line between an issue list and a comment on an existing provision in the draft uniform regulations is not necessarily clear cut. Nevertheless, I suggest that the working group include in the uniform regulations consideration of the following issues.

1. Definition of Unitary Business.

a. Instant unity. When is a newly acquired business unit unitary with the acquiring entity?

(1) Besides the usual factors such as general line of business, steps in a vertical enterprise, and strong centralized management, what consideration should be given to comparison of relationship between the acquired entity before and after acquisition?

(2) Should there be a presumption that no instant unity exists in the taxable period in which acquisition occurs?

(3) Should there be a presumption of lack of unity if no material changes in management personnel or conduct of the acquired enterprise occurs? If so, for how long?

b. Diverse business.

(1) Should there be a different standard for evaluating the role of strong centralized management where diverse businesses are involved, as opposed to business segments that are in the same general line of business or are steps in a vertically integrated enterprise?

(2) Should there be a distinction between (1) centralized housekeeping functions common to most enterprises, such as human resources management, internal audit, insurance, cash management, purchasing (for enterprises other than wholesaling or retailing enterprises), legal and tax administration, and (2) centralized management that is involved with day-to-day management of revenue producing activities involving provision of goods or services?

(3) Should the heightened prospects of misallocation of income where diverse business segments have dissimilar apportionment characteristics affect a unitary determination?

c. Flow-through entities.

(1) Should income be apportioned at the level of the flow-through entity, and passed along to members much like nonbusiness income, or should income be apportioned at the member level?

(2) Must the operation of the flow-through entity be unitary with a member before unity is established with the member, or is the unitary relationship established by reference to the relationship between the member and the interest of the member in the flow-through entity?

d. Uniform taxpayer reporting.

(1) Should any significance attach to a taxpayer's filing position in prior or subsequent years in a state?

(2) Should any significance attach to a taxpayer's filing position in other states that (a) have not adopted UDITPA substantially unchanged, or (b) have not adopted the uniform MTC unitary regulations?

2. Business-Nonbusiness Income.

a. Interest income; dividend income.

(1) Should there be a presumption that interest and dividend income from investments of funds in excess of the reasonable needs of the business activities of the taxpayer constitute nonbusiness income? For example, California auditors have used a Bardahl formula type analysis to divide passive income between a business income classification and a nonbusiness income classification.

b. Capital gains.

(1) Is gain or loss on the sale of property acquired to expand unitary business operations but never actually used in the unitary business properly classified as nonbusiness income?

(2) If a dealer in property holds similar or related property for long-term appreciation in value, is gain or loss on the sale of the investment property nonbusiness? If so, should the regulations provide standards for identification of nonbusiness investment property?

Very truly yours,


Roy E. Crawford

REC:si
Enclosure